Nos. 387-388

IN THE

Supreme Court of the United States

OCTOBER TERM, 1942

RECONSTRUCTION FINANCE CORPORATION,
Petitioner,

v.

BANKERS TRUST COMPANY, TRUSTEE,
Respondent.

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR RESPONDENT

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Statement

No separate statement of facts or of the question presented is set forth herein, since we are in accord with the statement of facts and with the statement of the question presented as contained in the brief for Petitioner, with the following (a) exception and (b) addition.

(a) We disagree with the last statement in the second full paragraph on page 3 of the Petitioner's Brief, that "it (the Indenture Trustee) has actively participated in such proceedings", but for the purpose of argument in this case we are willing to assume that the statement is correct.

(b) Bankers Trust Company, as Corporate Trustee (hereinafter called "Indenture Trustee") under the Refunding Mortgage of the Kansas City, Fort Scott & Memphis Railway Company, dated August 23, 1901 (hereinafter called the "Indenture"), now holds cash deposited with it subject to the terms of that Indenture in the amount of $475,127.71.

We are not replying to Point II of Petitioner's Brief that the term "Debtor's Estate" as used in Section 77(c)(12) embraces the total assets of the Debtor, or to Point III that the services rendered and expenses incurred by the Indenture Trustee and its counsel were rendered and incurred "in connection with the proceedings and plan", because the Circuit Court of Appeals in the case at bar has stated that the matters covered therein are not important or controlling on the decision of this case (Rec. pp. 105 and 106).

Summary of Argument

The Indenture Trustee has a contract right and prior lien upon the mortgaged property created by the Indenture as well as by the common-law, for its reasonable compensation for all services and expenses (including the compensation and expenses of its counsel) rendered and incurred in the execution of the trusts created by the Indenture. The institution of the Section 77 proceedings did not in any degree destroy or impair the validity, scope or extent of that contract right and lien, which covered all of the services and expenses which the Indenture Trustee was under a duty to render and incur for the protection of the trust estate and on behalf of the bondholders, after, as well as before, the inception of the Section 77 proceedings. The Indenture Trustee was not a

volunteer and has consistently denied that it was subject to the conditions of Subsection (c)(12) thereof. It intervened in those proceedings in response to its duties under the Indenture and has relied solely upon its contract claim and lien thereunder for its compensation and expenses.

The language and the legislative history of Section 77(c)(12) fail to show that Congress intended that statute to apply to the claim of an Indenture Trustee for compensation and expenses rendered and incurred in the execution of the trusts created by the Indenture, based upon a contractual right and secured by a lien conferred by the Indenture. There was no intent to transfer the Bankruptcy Court's established and exclusive jurisdiction to liquidate such a claim and lien to the Interstate Commerce Commission.

Section 77(c)(12) should be held not to apply to the Indenture Trustee since any decision to the contrary would render that statute unconstitutional for the following reasons:—

Section 77(c)(12), if held to apply to the claim of the Indenture Trustee, would be an unconstitutional denial of its right to judicial review, to which it is constitutionally entitled, since neither the Bankruptcy Court nor the Circuit Court of Appeals has any authority under Section 77(c)(12) or under Section 77(c)(2) to determine whether the reasonable value of the services and expenses of the Indenture Trustee exceeds the maximum allowances therefor fixed by the Commission, and neither of those Courts can take any effective action to have those maximum allowances raised.

Section 77(c)(12), if held to be applicable to the services and expenses of the Indenture Trustee, would be an unconstitutional impairment of its vested property

rights. Congress does not have the power to impair vested property rights by bankruptcy legislation. The application of the above statute does not constitute a mere suspension of or change in the Indenture Trustee's remedy, but constitutes an actual impairment of its substantive right to a lien and to have that lien liquidated under the standards to which it was entitled under its Indenture contract.

Subsection (c)(12) of Section 77, if held to be applicable to the services and expenses of the Indenture Trustee, would be a violation of Section 1 of Article III of the United States Constitution. The adjudication of the amount of the contract claim and lien of an indenture trustee for its compensation and expenses is a matter of private right and consequently a judicial function, which can be performed only by the courts and may not be delegated to the Commission.

ARGUMENT

Introductory Statement

The decision of the Circuit Court of Appeals in the case at bar (Rec. p. 102; reported in 129 Fed. (2d) 122) held squarely that the Bankruptcy Court had jurisdiction to allow the contract claim of the Indenture Trustee for its services and expenses rendered and incurred in the execution of the trusts, without the intervention of the Interstate Commerce Commission under Section 77(c)(12). The opinion rests upon the doctrine which it sets forth that since the Indenture Trustee had a contract claim and prior lien under the terms of the Indenture for compensation for services rendered and expenses incurred by it in the protection of the trust

estate and in the interest of its bondholders, it was entitled to have the Bankruptcy Court liquidate that claim without prior reference to the Commission under Subsection (c) (12) of Section 77. Furthermore, it concluded that this was so even though the services and expenses may have been rendered and incurred in connection with the reorganization plan and proceedings and may have been beneficial to the reorganization proceedings, which facts (said the Court) should add to, rather than detract from, its right to compensation. The core of its decision is contained in the following quotations from the opinion (Rec. p. 102):

p. 106:

"Appellee's claim is based upon its contract, expressed in the refunding mortgage, and is for its services to the trust estate required by that mortgage in fulfilling its duty and obligation to the bondholders secured by the mortgage.

Under Sec. 77 of the Bankruptcy Act the bankruptcy court acquired exclusive jurisdiction of all of the property of the debtor railroad wherever situated. But it took possession of the debtor's property subject to all valid claims against it. Appellee, as trustee under a mortgage conveying a large part of the debtor's estate as security for the payment of certain bonds of the debtor, intervened in the reorganization proceedings in order to protect the rights of the bondholders. In any plan of reorganization of the debtor finally adopted, these bondholders were entitled to fair and equitable treatment, and appellee was a proper party to represent them in the reorganization proceedings. By the terms of the trust indenture it was entitled to compensation for its services rendered in behalf of the bondholders. As a general rule the trustee is entitled to compensation out of the trust estate for

the services rendered and expenses incurred in the protection of the trust. Perry on Trusts and Trustees, Vol. II, p. 1531; Restatement, Law of Trusts, Vol. I, Secs. 242, 244. *Schoenherr* v. *Van Meter*, 215 N. Y. 548, 109 N. E. 625; *Hallett* v. *Moore*, 282 Mass. 380, 185 N. E. 474, 91 A.L.R. 572. In the present case the trust estate was charged with a lien to secure the payment for the trustee's services and expenses properly incurred in the administration of the estate. As the bankruptcy court had possession of the trust estate as a part of the debtor's estate, it was necessary for the appellee to apply to that court for the allowance of its claim.

Nor is the fact that the services of appellee may have been rendered and its expenses incurred in connection with the reorganization plan and proceedings controlling on the question here. In a literal sense they were because they were made necessary by the reorganization proceedings. The officers of appellee and its counsel gave attention to the steps taken in the proceedings and attended hearings before the court and the Commission. They took part in conferences in regard to the status of the proposed plan of reorganization and in meetings held to work out new plans. But appellee was at all times acting primarily in the interest of the bondholders under the refunding mortgage. The fact that the services of appellee on behalf of the trust estate were also beneficial to the reorganization proceedings should add to, rather than detract from, its right to compensation."

p. 107:

"• • • But the Commission was measuring the reasonable value of appellee's services in the reorganization proceedings to the estate of the debtor. Appellee is not asking for compensation for that service. On the other hand it asks reasonable com-

pensation for the value of its services to the trust estate."

* * * * * * * * * *

"We think the claim of the appellee was within the jurisdiction of the court below to allow without the intervention of the Interstate Commerce Commission under Sec. 77(c)(12)."

I

Section 77(c)(12) has no application to the claim of an Indenture Trustee for services and expenses rendered and incurred by it in the execution of the trusts, based upon contract and secured by a lien upon the mortgaged estate, and therefore does not apply to the claim of the Indenture Trustee herein.

A

The Indenture Trustee has a contract right and prior lien upon the mortgaged property for all of the services and expenses rendered and incurred by it in the execution of the trusts created by the Indenture.

There can be no doubt that the Indenture Trustee has a contract claim and prior lien upon the mortgaged property for its reasonable compensation and expenses (including the compensation and expenses of its counsel) for all services rendered by it in the execution of the trusts created by the Indenture. Article Twenty-third of the Indenture confers that right and lien in express terms as follows:

"The Trustees shall be entitled to reasonable compensation for all services rendered by them in the execution of the trusts hereby created, which compensation as well as all reasonable expenses necessarily incurred and actually disbursed hereunder, the Railway Company agrees to pay and hereby charges on the trust estate."

Furthermore, even in the absence of that provision of the Indenture, the Indenture Trustee would have that contract right and prior lien under the well-settled doctrine that a trust fund must bear the expenses of its protection and administration.

See:

Schoenherr v. *Van Meter*, 215 N. Y. 548 at pages 551-552 and cases there cited, 109 N. E. 625, (Ct. of Appeals 1915);

Hallett v. *Moore*, 282 Mass. 380, 185 N. E. 474, 480 (Sup. Jud. Ct. of Mass. 1933);

Restatement of the Law of Trusts, Vol. I, Sections 242 and 244;

Perry on Trusts, 7th Ed., Vol. II, at pages 1531, 1535-1536;

Rensselaer & Saratoga R. Co. v. *Miller & Knapp*, 47 Vt. 146;

McLane v. *Placerville & S. V. R. Co.*, 66 Cal. 606, 6 Pac. 748.

The lien created by a mortgage contract is not affected by the institution of a bankruptcy proceeding. See *Security Mortgage Co.* v. *Powers*, 278 U. S. 149 (1928), 153, 156.

Furthermore, the existence and validity of the particular kind of lien here involved, covering the compensation and expenses of an indenture trustee, have been upheld in Section 77 proceedings. See *In re New York, New Haven and Hartford Railroad Company, Debtor*, 46 Fed. Supp. 236 (U.S.D.C., Conn., June 3, 1942, set forth in full as Appendix B at p. 59 of Petitioner's Brief). That decision is hereinafter referred to as the "New Haven decision."

There is no basis whatsoever for the contention of Petitioner that the contract right and lien conferred by the Indenture upon the Indenture Trustee for its services and expenses are confined to foreclosure and fail to provide compensation for services performed by the Indenture Trustee occasioned by Section 77 proceedings (Petitioner's Brief, pp. 27-28).

Article Twenty-third of the Indenture, which gives the Trustees the right "to reasonable compensation for all services rendered by them in the execution of the trusts" created thereby, is phrased in the broadest possible terms and under it the Indenture Trustee's contract right and lien cover compensation for *all services* which the Indenture Trustee is required to render. Proceedings under Section 77, which was not enacted until thirty-two years after the date of the Indenture, obviously could not be specifically referred to in the Indenture, but that does not mean that services occasioned by such proceedings are not covered by it, since after default a trustee's powers and duties in the execution of the trusts are not restricted to the specific remedies which are outlined in detail in the Indenture. This is made clear by Article Fourteenth of the Indenture itself, which provides that in case of default, the trustees "may forthwith proceed to protect and enforce their rights and the rights of bondholders under this indenture by a suit or suits in equity or at law, either for the specific performance of any covenant or agreement contained herein, or in aid of the execution of any power herein granted, or for the foreclosure of this indenture for interest or for principal and interest, or for the enforcement of any other appropriate legal or other equitable remedy, as the Trustees shall deem most effectual in support of any of their rights or duties hereunder."

Mortgages seldom, if ever, have contained a provision that, in the event of an equity receivership, the trustee shall participate in the receivership proceeding and look after the interests of the bondholders; but, nevertheless, it will scarcely be asserted that the trustee has no duties in such event.

Mortgages could not have defined the various duties which trustees have after default, including in specific detail those to be imposed by future legislation not conceived at the time of execution of the mortgage, without possession of prophetic or clairvoyant powers by the author; but the failure to define duties does not excuse their non-performance. In *Frishmuth* v. *Farmers' Loan & Trust Co.*, 95 Fed. 5 (C.C.S.D.N.Y. 1899), the court said at page 8:

> "• • • The duties assumed by one to whom a railroad mortgage is made for the benefit of bondholders are not those only which are defined by the terms of the instrument. Others are superimposed upon the trustee, created by the relation of the parties and the situation of the trust fund. Although selected by the mortgagor, the trustee is selected to represent as well those who may become the holders of bonds. No one but the trustee can enforce the covenants and conditions of the mortgage, or take proper measures to protect the interests of bondholders in respect to matters not provided for by the terms of the instrument."

See also *In re Denver & R. G. Western R. Co.*, 13 Fed. Supp. 821 (D.C.D. Colo., 1936) in which it has been specifically held that indenture trustees are required to protect the interests of their bondholders in Section 77 proceedings.

It is clear from the foregoing that the terms of the Indenture as to compensation and expenses are broad enough to cover all services and expenses which the Indenture Trustee was required to perform and incur, including its services and expenses occasioned by the Section 77 proceeding.

Petitioner contends (Brief, pp. 28, 35) that the Indenture Trustee had an unfettered option to resign its trust, but instead voluntarily elected to participate in the Section 77 proceedings with knowledge of the provisions of that statute to which it was therefore subject. It is evident therefrom that Petitioner fails to appreciate the fundamental distinction between indenture trustees and volunteers in Section 77 proceedings.

The Indenture Trustee accepted its duties and responsibilities in 1903, long prior to the enactment of Section 77. Those duties involved the execution of the trusts and the protection of the interests of the bondholders, and after default they ripened and became active and responsible. Can Petitioner be arguing that the Indenture Trustee was entitled to abdicate its duties in the execution of the trust, at the very time when their active performance had become most urgent and imperative, merely because by way of innovation a statutory type of reorganization procedure had been created by Section 77? That statute does not in the slightest purport to limit the responsibilities and duties of the Indenture Trustee and the latter could not, of course, voluntarily limit them. On the contrary, the policy of the Congress, as shown by the Trust Indenture Act of 1939, is to require indenture trustees to be vigilant notwithstanding the enactment of Section 77. Section 315(c) of that Act, 15 U.S.C.A., Sec. 77ooo(c), reads as follows:

"Duties of the Trustee in Case of Default.

"(c) The indenture to be qualified shall contain provisions requiring the indenture trustee to exercise in case of default (as such term is defined in such indenture) such of the rights and powers vested in it by such indenture, and to use the same degree of care and skill in their exercise, as a prudent man would exercise or use under the circumstances in the conduct of his own affairs."

Petitioner's position was flatly rejected by the District Court in the New Haven decision (see pp. 60-61 of Appendix B of Petitioner's Brief), as follows:

"I cannot accept the view that the petitioners were acting as mere volunteers in the premises. • • •

I think no one will dispute that the petitioners would have been remiss in their proper discharge of their trusts if in an equity receivership they had left their cestuis without representation or after default had failed to take appropriate action for their protection. Certainly this equitable obligation was not precisely to be measured by their possible liability in an action at law for nonfeasance. I find nothing in Section 77 which exonerates mortgage trustees from their equitable obligation to take action appropriate to the same objective. Such a view, indeed, seems repugnant to Congressional policy as declared in the Trust Indenture Act of 1939. See 15 U.S.C.A. §§77bbb and 77ooo(c).

• • • this change did not extinguish any rights or obligations growing out of the mortgage indenture nor transform the status of the petitioners from that of responsible trustees to that of volunteers."

Since the Indenture Trustee was not a volunteer, but took the only course open to it in order to protect the interests of its bondholders, there is no substance to Petitioner's contention (Brief, p. 28) that it subjected itself to the conditions of Section 77(c)(12) (Rec. p. 84).

Contrary to the suggestion of Petitioner (Brief, p. 28), the fact that the Indenture Trustee's services were rendered after the date of bankruptcy does not diminish the validity or extent of the lien for compensation for such services. See *Security Mortgage Co.* v. *Powers*, 278 U. S. 149, 156 (1928), where the court stated concerning a contract for attorneys' fees in a mortgage:

> "• • • The lien was not inchoate at the time of the adjudication. It had already become perfect when the principal note and the loan deed securing it were given. Property subject to a lien to secure a liability still contingent at the time of bankruptcy is not discharged from the lien by the adjudication. The secured obligation survives; and if it is that of a third person is usually unaffected by the bankruptcy. When by the happening of the event the contingent liability becomes absolute, the lien becomes enforceable though this occurs after the adjudication."

See also:

In Re American Motor Products Corporation, 98 Fed. (2d) 774, 775 (C.C.A. 2, 1938).

B

Subsection (c)(12) of Section 77 does not apply to the claim of an indenture trustee for its services and expenses in the execution of the trusts, based upon contract and secured by a lien upon the mortgaged estate.

There is no doubt that prior to the enactment of Section 77(c)(12) the authority to determine the validity, amount, extent and priority of that kind of contract claim and lien had always been vested exclusively in the courts.

It is our position (which has been sustained by the decision of the Circuit Court of Appeals in the case at bar) that Section 77(c)(12) was not intended to apply to the liquidation or enforcement of that kind of contract claim and lien and was not intended to transfer to the Commission the Bankruptcy Court's established and exclusive jurisdiction to liquidate such claim and lien. That position is based upon the following:

(1) The Indenture Trustee's secured claim and lien for its compensation and expenses are exactly like any other claim and lien except that no right is conferred to vote upon the plan. No different treatment is provided for them under Section 77 than for any other claim and lien.

The amount, extent and priority of all secured claims and liens are intended under Section 77 to be adjudicated solely by the Bankruptcy Court and not by the Commission. Subsection (c)(7) provides expressly that the judge shall determine and fix a time within which claims of creditors may be filed and "the manner in which such claims may be filed or evidenced and allowed," and further provides for the division by the judge of creditors and stockholders "into classes according to the nature of their respective claims and interests." An indenture trustee's secured claim and lien are just like any other claim and lien. They are among those for which the plan

of reorganization must provide (Section 77(b)(3); and for which provision must be made before the property may be transferred "free and clear", and before the mortgagee may be required to discharge the mortgage lien (Section 77(b)).

(2) There is a fundamental distinction between compensation under an indenture contract claim and lien for services in the execution of the trusts created by the indenture, and an allowance out of the debtor's estate under Section 77(c)(12) for services in the reorganization proceedings to the estate of the debtor.

Subsection (c)(12) is in terms applicable only to an "allowance to be paid out of the debtor's estate." The Indenture Trustee is not applying here for an "allowance" out of the Debtor's estate under Subsection (c)(12); and its rights do not arise by reason of Section 77(c)(12), but wholly independently thereof. It is seeking to enforce a contract right and a lien therefor conferred upon it both by the Indenture and by the common law in 1903, thirty years prior to the enactment of Section 77 itself.

As stated by the Circuit Court of Appeals in the case at bar (Rec. p. 107):

> "• • • But the Commission was measuring the reasonable value of appellee's services in the reorganization proceedings to the estate of the debtor. Appellee is not asking for compensation for that service. On the other hand it asks reasonable compensation for the value of its services to the trust estate."

The courts have several times recognized the distinction under Section 77B between compensation of an inden-

ture trustee under a contract claim and lien created by the indenture, and an allowance out of the debtor's estate.

Thus, in *Straus* v. *Baker Co.*, 87 Fed. (2d) 401 (C.C.A. 5, 1937), the court clearly distinguished between the right of an indenture trustee to an allowance from the general estate and his right to compensation under the terms of the mortgage from a fund available for bondholders, stating, at page 408:

> "The trustee Straus makes claim in the dual capacity of trustee for the bondholders under the mortgage, and as reorganization trustee. If, as the court found, he was active in the matter of the National Hotel cash plan; and those activities were in the interest of the bondholders, and contrary to the interest of the estate as a whole, the court correctly denied him compensation as reorganization trustee. But as trustee for the bondholders he was in any event entitled under the mortgage contract, to an allowance out of the fund."

The same distinction has been recognized in the case of *In re Buildings Development Co.*, 98 Fed. (2d) 841, 843-844 (C.C.A. 7, 1938), in which it was held that if a mortgage trustee does not "claim any priority . . . by reason of the lien provision in the trust indenture", and seeks only an allowance from the general estate, the burden is upon such trustee to show the value of its services "to the debtor apart from the value to the bondholders".

This distinction is clearly recognized by the Circuit Court of Appeals in the case at bar. Thus it said (Rec. p. 106-107):

> "There is nothing in the case of *In re Chicago and N. W. Ry. Co.*, D. C., 35 F. Supp. 230, 250, contrary to the opinion expressed here. In that case the

> trustees under a refunding mortgage were asking compensation, not under the terms of the mortgage, but under Sec. 77(c)(12) of the Bankruptcy Act. The court properly held that it was without jurisdiction to allow them more than the maximum amount fixed by the Interstate Commerce Commission regardless of whether they were to be paid from the general estate of the debtor or from the property pledged to secure the mortgage under which they were trustees. On the other hand, in *Straus* v. *Baker Co., supra*, a proceeding under Sec. 77B of the Bankruptcy Act, the court held that a trustee under a mortgage was entitled to compensation out of the property pledged under the mortgage for services to the trust estate."

See the further quotations from its opinion, set forth at pages 5-7, *supra*.

There is no evidence in either the history or the language of Section 77(c)(12) that Congress intended to abolish the above distinction and to make an application for an allowance under that statute the exclusive remedy for compensation of indenture trustees for services in the execution of their trusts and for expenses, for which they have a lien.

(3) The inclusion of the phrase "trustees under indentures" in Section 77(c)(12) does not require any other conclusion. It gives compensation to an indenture trustee who might otherwise receive none, such as a trustee under an unsecured issue or a trustee whose security has no value. But a trustee is not limited to the remedy of an allowance pursuant to Subsection (c)(12) and is not compelled to surrender its contract right to obtain its compensation from the liquidation of its lien by a court. The right conferred by that statute is not man-

datory, but a privilege of which a trustee may take advantage if and to the extent that it falls within the requirements of the statute. In this connection it will be observed that the language of Subsection (e)(12) is permissive in terms. It provides only that the judge "may make an allowance"; he is not required to do so. Thus in *In re A. Hrrtz, Inc.*, 84 Fed. (2d) 511 (C.C.A. 7, 1936), the court in construing Subsection (e)(9) of Section 77B, which is substantially identical with the phraseology of Section 77(e)(12) here involved, said at page 513:

> "The statute defines the groups that *may* be compensated but this in no sense is to be construed as meaning *shall* be compensated."

See also *Teasdale* v. *Sefton Nat. Fibre Can Co.*, 85 Fed. (2d) 379 (C.C.A. 8, 1936) at page 382.

The distinction between permission to apply for an allowance on the one hand and on the other hand a contract right to compensation, secured by a lien, speaks for itself. Much more specific language than the statute contains is required, we submit, to show that Congress intended to substitute the former for the latter and to deprive a trustee of its pre-existing contract and lien claim for services performed in the interest of the trust estate and the bondholders, and to abrogate the legal incident of that claim: *viz.*, liquidation by the Bankruptcy Court.

The foregoing construction of Subsection (e)(12), which gives an indenture trustee a privilege to avail itself of that statute, but which does not compel it to surrender its right to have its lien liquidated by a court, not only gives full effect to the specific terms of the statute, but (unlike the construction argued for by Petitioner in its

Brief at pages 11-16) also gives (1) full recognition to the status of the Indenture Trustee as a secured creditor under Section 77 with rights equal to all the other secured creditors thereunder and (2) full recognition to the well defined distinction between compensation under a contract claim and lien, and an application for an allowance.

(4) Congress did not intend that Subsection (c)(12) of Section 77 should be applicable to the Indenture Trustee and result in the impractical and unworkable situation suggested in the New Haven decision. In that decision the Court said (p. 63 of Appendix B of Petitioner's Brief): "And if the Judge shall not be satisfied that such maxima permit of allowances which are reasonable, under the Act the Judge may return the petition for reconsideration by the Commission. * * * To be sure this seems a cumbersome procedure for the liquidation of an allowance. Indeed, theoretically at least, the procedure may produce a deadlock between the Commission and the Judge which may ultimately block a reorganization. * * * And if ever a case shall arise resulting in a final deadlock instead of agreement, *perhaps* the disagreement can be solved by an appeal from the Judge's order disapproving the reasonableness of a reconsidered maximum set by the Commission." (Italics ours.)

The procedure set forth above by the District Judge in the New Haven decision would almost certainly produce any one or more of the following results: (1) a game of battledore and shuttlecock between the Judge and the Commission, (2) a deadlock between them, or (3) the ultimate blocking of the reorganization of the Debtor. Congress certainly could not have intended that Subsection (c)(12) of Section 77 should result in any of those situations. Nor is the possibility of those results so

theoretical as suggested by the Judge. It is quite conceivable that District Judges with views divergent from the Commission's as to the measure of reasonable compensation might frequently find it impossible to come to an agreement with the Commission on the subject. No better illustration of the possibility of such a deadlock could be found than the case at bar, in which the maximum allowances fixed by the Commission for the Indenture Trustee and its counsel aggregate less than one-third of the total compensation granted to them by the Court. The District Court in the New Haven decision finds no way out of such a dilemma, except that it says: "perhaps the disagreement can be solved by an appeal from the Judge's order disapproving the reasonableness of a reconsidered maximum set by the Commission." Apparently that is also the only way out of the dilemma that the Petitioner can suggest (Brief, p. 32). No appeal lies from Judges' orders disapproving the reasonableness of reconsidered maxima set by the Commission, because such orders do not constitute "orders of the Court fixing such allowances", which are the only orders appealable under Subsection (c)(12).

Petitioner sets forth various parts of Section 77 (Brief, pp. 37-59 of Appendix A) and refers to reports of Congressional Committees and discussions in Congress (Brief, pp. 13-14) which it alleges show that the purpose of Congress in enacting Section 77 and particularly Subsection (c)(12) thereof was to keep the reorganization costs within reasonable bounds and to prevent extravagance. We do not, of course, deny that policy, which required no such lengthy demonstration. What we do emphatically deny is that Congress, in order to accomplish that purpose, meant to take away the pre-existing jurisdiction of

the Bankruptcy Court over the liquidation of liens for compensation and to confer that jurisdiction upon the Commission. In this connection, we call the Court's attention particularly to the fact that of the five instances of jurisdiction purported to be conferred by Section 77 in connection with compensation (referred to by Petitioner at pp. 9-10 of its Brief), three of them involve jurisdiction conferred upon the Court and not upon the Commission.

We have no quarrel with the above-mentioned statements in Congress, as applicable to the granting of allowances to various parties who have no claim to compensation other than that provided for in that statute. But there is nothing whatsoever in any of those statements to show that Congress had in mind and intended Section 77(c)(12) to cover indenture trustees whose claims to compensation were secured by a lien created in good faith long prior to its enactment and to transfer the District Court's established jurisdiction over the determination of such a claim and lien to the Commission.

Certainly the case of *United States* v. *Chicago, Milwaukee & St. Paul Railway*, 282 U. S. 311 (1931), referred to by Petitioner (Brief, p. 12) does not furnish the slightest indication that Congress was aiming at such an indenture trustee. There the agreement was an obvious device entered into during and as a part of the reorganization proceedings, the purpose and effect of which were to raise a fund for the payment of compensation by compulsory contributions from the stockholders and to vest in the reorganization managers and various committees complete control of the amount of their compensation payable from that fund, free from all supervision not only of the Commission *but of any court*. Here the In-

denture Trustee has a lien based on a provision in the Indenture entered into in good faith, not during reorganization but long prior to the enactment of Section 77; that provision was not a device to accomplish a particular purpose in a special situation, but was included in substantially similar form in every corporate mortgage before and since that time. The Indenture Trustee is not seeking to evade the jurisdiction of the Court, but is asking the Court to determine the amount of its compensation and expenses.

Nor is the fact, that Section 77 subjects bondholders to the provisions of a plan of reorganization, which is relied upon by the District Court as an analogous situation in the New Haven decision (see pp. 61-62 of Appendix B of Petitioner's Brief), any indication that Section 77 intended to subject the secured claims of indenture trustees for compensation and expenses to the provisions of Subsection (c)(12), since the distinctions between the two situations are clear: (1) the bondholders have a lien the amount of which is definitely fixed by the terms of their indenture contract, while the amount of the lien of indenture trustees has to be determined; (2) the bondholders have been given the additional protection, under the statute, of a two-thirds vote of their particular class before they can be subjected to the plan, and of a clear-cut and established right of appeal while indenture trustees with a lien have no such right to vote and no right of appeal.

The Commission has no jurisdiction unless clearly conferred upon it by Section 77. See *In re Chicago & N. W. Ry. Co.*, 121 Fed. (2d) 791 (C.C.A. 7, 1941), in which the court, in referring to Subsection (c)(12), said at page 800:

"* * * Moreover, the jurisdiction is in the court, unless taken from it and placed in the I.C.C. by this subsection of the statute."

We submit that opposing counsel have failed to show that Section 77(c)(12) was intended to accomplish that transfer of jurisdiction in respect to indenture trustees holding liens who ask the Bankruptcy Court to liquidate their liens for services and expenses in the execution of the trusts, and that the decision of the Circuit Court of Appeals was correct in holding that the statute does not apply to such an indenture trustee.

That conclusion has been flatly supported in the following decision. In the Report dated December 3, 1940, of William L. West, Esq., Special Master appointed by the District Court in the Erie Railroad Company Reorganization in the District Court of the United States for the Northern District of Ohio, to pass on the claim of the Chase National Bank, a secured noteholder, for legal expenses incurred by it in the enforcement and protection of the collateral securing the note, but not in connection with the proceedings and plan, it was argued against the allowance of that claim that the court had no power to determine the Bank's claim for legal expenses without first referring the matter to the Commission for the fixing of a maximum amount under Section 77(c)(12). The Special Master rejected that contention completely, saying in his report:

"Furthermore, this claim involves the adjudication of a substantive right created by contract, for the Bank's right to have its reasonable expenses, including counsel fees, allowed as part of its secured claim arises by virtue of contract—i.e., the terms and provisions of the Debtor's note—and not by

virtue of the provisions of the Bankruptcy Act relating to 'allowances'. Thus, apart from the terms of the Debtor's note, the Bank would not be entitled in this proceeding to the allowance of its claim for expenses.

Under the circumstances, this claim is not compensable as an 'allowance' under the Bankruptcy Act so as to require action by the Commission with regard to the fixing of a maximum amount."

It should be noted that in *Matter of the Fort Dodge, Des Moines & Southern Railroad Co.*, referred to at page 10 and in Appendix C of the Petitioner's Brief, counsel for the indenture trustee, The New York Trust Company, did not appear and argue the case or file a brief.

Furthermore, as shown hereinafter under points II A, B and C (pp. 25-50), if Section 77(c)(12) is held to be applicable to the Indenture Trustee having a claim secured by a lien, it would render that Subsection of the statute invalid as an unconstitutional denial of its right to judicial review and as an unconstitutional impairment of its property rights, all in violation of the Fifth Amendment of the Constitution of the United States, and as a violation of Section I of Article III thereof. The Court below was right in construing Section 77(c)(12) as not applicable to the Indenture Trustee, since a contrary construction would render it unconstitutional.

The Court below did not pass on the constitutional points, because they were pertinent only if the intent of Section 77(c)(12) had been construed to require the judge to permit the Interstate Commerce Commission to fix the maximum limits of the compensation and expenses of the Indenture Trustee. The District Court in the New Haven decision, however, construed the intent of Section 77(c)(12) to require the judge to permit the Commission to fix

the maximum limits of such compensation and expenses in the first instance and held that there was no basis for the constitutional objections, which were the same objections as are raised in this proceeding. So far as we can ascertain, no other court has specifically passed upon these constitutional objections.

II

The decision of the Circuit Court of Appeals should be upheld, since any decision which should hold that Section 77(c)(12) was applicable to the Indenture Trustee would render that statute unconstitutional.

A

Subsection (c)(12) of Section 77, if held applicable to the Indenture Trustee, would be an unconstitutional denial of its right to judicial review in violation of the Fifth Amendment of the Constitution of the United States.

It is our contention, that if the maximum limits are to be fixed by the Commission under Subsection (c)(12), we are constitutionally entitled to a review of such maxima by some court, either the District Court or an Appellate Court, *with power to raise those maximum limits. We contend that no such right of review exists.*

Although the District Court is given the authority under that statute to make an allowance which may be less than the maximum fixed by the Commission, it is clear from the following authorities that the District Court has no power to pass upon whether the reasonable value of the services exceeds that maximum and that it may not raise that maximum.

Thus, in *In re Chicago, M., St. P. & P. R. Co.*, 121 Fed. (2d) 371 (C.C.A. 7, 1941), the court, after a study of Section 77(c)(12) itself and the history of the Congressional Records leading to its passage, said at page 374:

> "Our reading of the statute convinces us that Congress contemplated a plan (which it enacted) whereby the I.C.C., not the District Court, should fix the maximum allowances to attorneys; and within that allowance the court was to exercise its judgment.
>
> "• • • The court was ultimately to determine the amount of the fees, but its action was limited by the maximum fixed by the Commission."

In *In re Chicago & N. W. Ry. Co.*, 35 Fed. Supp. 230 (D.C.N.D. Ill., 1940), the court said at page 258:

> "But whether the reasonable value of the services exceeds the maximum limits fixed by the Commission is, so far as this court is concerned, an academic question which this court has no power to determine and which it accordingly must decline to examine."

See to the same effect the opinion in *Warren* v. *Palmer* (C.C.A. (2d) October 8, 1942, not yet reported), portion quoted at page 35 hereof; *In re Chicago, G. W. R. Co.*, 29 Fed. Supp. 149 (D.C.N.D. Ill., 1939), at page 162 and *Chicago and North Western Railway Co.* v. *United States of America, et al.* (Civil Action No. 2810 D.C.N.D. Ill., May 29, 1941, not yet reported) portion quoted at page 35 hereof.

Those decisions leave no doubt that the District Court has no jurisdiction whatsoever over the adequacy of the maximum and cannot take any effective action to have it

raised. Contrary to the contention of the Petitioner (Brief, pp. 10 and 29), those decisions are not in accord with the New Haven decision discussed below.

In the New Haven decision, the District Court rejected the theory of those cases and held that if it determined that the maximum set by the Commission was less than reasonable it could, as part of its authority over the plan of reorganization under Subsection (e)(2) of Section 77, return the petition for reconsideration by the Commission. It concluded that therefore the Indenture Trustee was not unconstitutionally deprived of its right to judicial review (see pp. 64-65 of Appendix B of Petitioner's Brief). Petitioner makes the same point in its Brief (see pp. 31-33).

Subsection (e)(2) provides as follows:

> "* * * After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: * * * (2) the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, *are within such maximum limits as are fixed by the Commission, and are within such maximum limits* to be subject to the approval of the judge; * * *" (Italics ours.)

We submit that the foregoing interpretation of that Subsection adopted by the District Court in the New Haven decision and by Petitioner is erroneous for the following reasons:

(1) Plainly that interpretation is contrary to the foregoing cases which hold that the exercise of the Court's judgment as to allowances is limited absolutely by the

maximum fixed by the Commission and that the Court has power only to diminish that maximum.

(2) The interpretation of Subsection (e)(2) by the District Court in the New Haven decision and by Petitioner is clearly contrary to the intent of Congress in enacting that Subsection, as shown by the language and history thereof.

Subsection (e)(8) of Section 77, as enacted March 3, 1933, provided that the judge might, within such maximum limits as should be fixed by the Commission as elsewhere provided in Subdivision (f) of Section 77, allow a reasonable compensation for services rendered and reimbursement for actual and necessary expenses incurred in connection with the proceeding and the plan. Subsection (f) provided that the Commission should fix the maximum compensation and reimbursement which might be allowed by the court pursuant to Subsection (e)(8). Subsection (g), which was the predecessor of the present Subsection (e)(2), provided that the judge should confirm the plan if satisfied that "all amounts to be paid by the debtor or by any corporation or corporations acquiring the debtor's assets, for services or expenses, incident to the reorganization and cost of financing, have been fully disclosed *and are reasonable*, or are to be subject to the approval of the judge." (Italics ours.) It will be observed that there was no reference therein to "maximum limits". Thus, if the District Court in the New Haven decision had been construing the old Subsection (g) instead of its present version (e)(2), its conclusions might be supported.

Subsection (e)(2), however, which superseded the foregoing Subsection (g) in the 1935 Amendments to Section 77, provides that the judge shall approve the plan, if

satisfied that the allowances are "* * * reasonable, *are within such maximum limits as are fixed by the Commission and are within such maximum limits to be subject to the approval of the judge;* * * *".* (Italics ours.)

The Court will note that in order to make sure that the limitation contained in Subsection (e)(12), in regard to maxima, which was not contained in the old Subsection (g), was carried over into the present Subsection (e)(2), the phrase "are within such maximum limits" was inserted *twice* in Subsection (e)(2).

Thus the interpretation placed upon Subsection (e)(2) by the District Court in the New Haven decision and by Petitioner is specifically negatived by the language of that provision and the history of its enactment, both of which show an emphatic determination on the part of Congress to prevent that interpretation and to make Subsection (e)(2) conform to Subsection (e)(12) in confining the authority of the District Court within the maxima fixed by the Commission.

(3) The interpretation of Subsection (e)(2) by the District Court in the New Haven decision and by Petitioner is also contrary to the intent of Congress in enacting Subsection (e)(12), as shown clearly by the discussion in the Senate and by the testimony at the hearings before the House Judiciary Committee, leading to its passage.

Thus the following discussion occurs in the Senate on consideration in 1933 of paragraph (e)(8), predecessor of the present Subsection (e)(12) (76 Cong. R. 5130):

> "Mr. LaFollette: Mr. President, the amendment to which the Senator refers provides, I understand, that the maximum limit shall be set by the Interstate Commerce Commission and within that

maximum limit the district judge may fix the commissions.

Mr. Clark: But the court can not go above the amount fixed by the commission.

Mr. LaFollette: That is correct. I said 'within the maximum limit.'

Mr. Robinson of Arkansas: The Senator is correct. The Interstate Commerce Commission ascertains what will be the maximum amount to be allowed, and the court within that limit may make the allowance."

In the colloquy in which Commissioner Mahaffie of the Commission was testifying as to Section 77(c)(12) at the hearings in April, 1935, before the House Judiciary Committee on the proposed amendments to Section 77 (quoted by the Court in *In re Chicago, M., St. P. & P. R. Co.*, 121 Fed. (2d) 371, *supra*, at p. 374), it was stated:

"Mr. Celler (Member of the House Judiciary Committee): It is true, though, that the court has very little to do under those circumstances.

Mr. Mahaffie: The court has to fix the actual fee and may have to hold a hearing on it.

Mr. Hancock (Member of the House Judiciary Committee): You anticipate that the maximum fee fixed will be the fee allowed and will also be the minimum fee, do you not? In other words, there will be no discretion left to the judge at all, as a matter of fact.

Mr. Mahaffie: I would not want to say that the court would not use some discretion under the statute. I anticipate that we will be the limiting factor on fees, however, if this proposed law is passed.

Mr. Celler: For practical purposes there would be no discretion left in the court except as to your maximum which would be quite low, I imagine, considering all the facts.

Mr. Mahaffie: I think that is substantially what has happened under section 77 as to the fixing of salaries; yes sir. We have fixed which we called a maximum and I think the courts have almost uniformly paid it."

From which the Circuit Court of Appeals in that case concluded as follows:

"Our reading of the statute convinces us that Congress contemplated a plan (which it enacted) whereby the I.C.C., not the District Court, should fix the maximum allowances to attorneys, and within that allowance the court was to exercise its judgment. * * *

To accomplish the result thus sought, the I.C.C. was empowered (and required) to fix the ceiling,—the maximum of fees and expenses for the various counsel representing the numerous claimants. The court was ultimately to determine the amount of the fees, but its action was limited by the maximum fixed by the Commission."

In the Report of the same hearings, the following occurred at page 85:

"Mr. Burgess (counsel for insurance companies): * * * I am not sure whether that maximum is appealable. Are you, Mr. Craven? That is, can the fixation of a maximum by the Commission be appealed under this act?

Mr. Craven (counsel for Commissioner Eastman in drafting the 1933 Act): I think not.

Mr. Burgess: You think not?

Mr. Craven: That is my recollection of it.

Mr. Celler (Member of the House Judiciary Committee): Even if the court would accept the maximum there would be no appeal from the court's ruling?

Mr. Burgess: I do not know of any appeal that you can take from the Commission's fixation of a maximum under this act.

Mr. Celler: That does not seem right.

Mr. Burgess: That is an appeal from the court's fixation, of course, but that would have to be within the maximum, so I do not know of any appeal.

. . . . . .

Mr. Celler: That leaves the entire matter in the hands of the Interstate Commerce Commission, practically speaking.

Mr. Michener: Yes.

Mr. Burgess: Yes.

Mr. Celler: With no right of appeal at all if the maximum is accepted by the court?

Mr. Burgess: That is my understanding. If Mr. Craven has a different view, I should be glad to accept his view.

Mr. Craven: That is my understanding of it."

Thus the language of Subsection (c)(12), its history, the announced intention of Congress in enacting the legislation and all of the decisions construing the same (except the New Haven decision) are uniform in showing that the Commission was intended to be the limiting factor on allowances and that the authority of the District Court to exercise judgment in the matter was to be confined within the Commission's maxima. It follows that in so far as Subsection (c)(2) of Section 77 appears to give the Court the right to pass upon reasonableness, the Court is confined thereunder to determining whether the fixed limits are unreasonably high, and that it has power only to diminish the allowances. The decision of the District Court in the New Haven matter, whereby the Court purported to have the power to exercise a veto over all of

the Commission's maxima on the ground that they were unreasonably low, is equivalent to a holding that the Court itself has power under Subsection (c)(12) to fix the allowances and is therefore directly contrary to the intent of the statute and, we submit, is erroneous, since it in effect vests final control over their amount in the Court instead of in the Commission.

There is a fundamental distinction between the power of the District and Circuit Courts over a plan of reorganization, and their power to review maximum limits of allowances. Under the former the courts are not bound by the plan proposed by the Commission. If one plan or fifty plans submitted by the Commission appear to the courts to be unreasonable, one and all can be rejected by the courts. Under Subsection (c)(12), on the contrary, if the Commission should allow a maximum of $50 for services which the Court considered to be worth $10,000, the Court could do nothing to raise the maximum or to compel the Commission to do so.

The right of appeal to the Circuit Court of Appeals furnished by Subsection (c)(12) does not satisfy the requirements of judicial review, because that right is confined to appeals from "orders of the Court fixing such allowances." That subsection furnishes no authority whatever for an appeal from the maximum fixed by the Commission, and that authority is not contained anywhere in the statute. See to that effect testimony of Mr. Burgess and Mr. Craven before the House Judiciary Committee set forth at pages 31-32, *supra*. On appeal from the District Court's orders, the Circuit Court of Appeals cannot determine whether the maximum is unreasonably low, since the District Court in making the order appealed

from cannot pass upon that question. Thus in *Warren* v. *Palmer, supra*, which involved the question whether attorneys who appeal from the order fixing their allowance under Section 77(c)(12) must obtain leave to appeal or may do so as of right, the Circuit Court of Appeals said:

> "• • • for in no case can an attorney in a railroad reorganization receive more than the maximum fixed by the Interstate Commerce Commission under §77(c)(12); so that in practice the only issue which such appeals can raise is whether the district judge was wrong in not awarding the whole or some part of the difference between the 'ceiling' fixed by the Commission and the amount which he did award. • • •"

As shown by all of the foregoing, both the District Court in making its order and the Circuit Court of Appeals in reviewing it are confined under Subsection (c)(12) to a determination of reasonableness within the maximum fixed by the Commission.

Contrary to the contention of Petitioner (Brief p. 32), there is nothing whatever in the statute which authorizes the Circuit Court of Appeals to remand any finding on maximum allowances to the Commission at any stage of the proceedings. Even if that were possible, the Court would be powerless to fix the sum to be awarded and the Indenture Trustee's only remedy would consist of a succession of expensive appeals to the Circuit Court of Appeals from successive inadequate maxima fixed by the Commission.

Contrary to the contention of the Attorney for the Trustees of the New Haven Railroad, contained at pages 7-9 of his brief *Amicus Curiae* filed herein, there is no right of appeal under the Urgent Deficiencies Act from the maximum limits fixed by the Commission. See *Chicago*

and North Western Railway Company v. *United States of America, and Interstate Commerce Commission* (Civil Action No. 2810 D.C.N.D. Ill., May 29, 1941, not officially reported), which arose on an appeal to a statutory three-judge court under the Urgent Deficiencies Act, for an injunction setting aside an order of the Commission which refused to make an allowance for the costs of an appeal by the debtor therein from the approval of the plan of reorganization. There the court in holding that it did not have jurisdiction of the appeal said in referring to Section 77(c)(12):

> "This section provides a complete scheme for the handling of expenses of reorganization—first, the I.C.C. passes upon the maximum amount which may be devoted to a specific expense, then the district court further checks such allocation, *and is granted power only to diminish the same; and then the aggrieved party may challenge the District Court's determination* by immediate and summary appeal to the Circuit Court of Appeals." (Italics ours.)

See also *Warren* v. *Palmer*, referred to at page 34, *supra*, in which the court said "*for in no case can an attorney in a railroad reorganization receive more than the maximum fixed by the Interstate Commerce Commission under Section 77(c)(12);* * * *." (Italics ours.)

Nor is the remedy of mandamus available to determine whether the Commission has made a reasonable allowance, since it is axiomatic that mandamus will not lie to control or review the exercise of discretion (in the absence of patent abuse).

From all the foregoing, we submit that there is no right of judicial review from the Commission's maxima with power in the Court, directly or indirectly, to raise them and that the District Court's conclusion in the New

Haven decision, that the Indenture Trustee's constitutional right to judicial review has been safeguarded, is clearly unsound. That the Indenture Trustee has a right to judicial review as to other aspects of allowances of compensation (Petitioner's Brief, page 33) does not, of course, cure that constitutional deficiency, but merely emphasizes it. That the District Court and the Circuit Court of Appeals can revise the maximum downward, or make no allowance at all, is not germane to the issue here presented.

Of course, the right to a rehearing before the Commission (Petitioner's Brief, p. 30) does not satisfy the constitutional right of the Indenture Trustee to a determination by a court. Two or more hearings by an administrative body are not the equivalent of one court hearing.

Petitioner's references to "coordinated regulatory power" (Brief, p. 14) and "coordinated action" (Brief, p. 32) of the Commission and of the court, under Subsection (c)(12), are not accurate descriptions of the real situation since they suggest equality of authority between these two tribunals, whereas, as shown above, under Subsection (c)(12) complete and exclusive control of maximum allowances is vested in the Commission and the court is confined to action subordinate to and limited by those maxima.

Since Subsection (c)(12) makes no provision for any judicial review *upward* from the maximum of the Commission, which is binding and conclusive, it is unconstitutional if held to be applicable to the determination of the contract right and lien of the Indenture Trustee for compensation and expenses.

We conclude therefore that the court below was right in construing Section 77(c)(12) as not applicable to the Indenture Trustee, since a contrary construction would render it unconstitutional.

It is well established that legislation, whether of Congress or of the States, cannot constitutionally make the determination of an administrative body binding and conclusive in a matter involving a constitutional question and take away the right to the independent review of a court. In the case at bar the constitutional matter involved is the Indenture Trustee's claim and lien for reasonable compensation and expenses (to be determined according to the recognized standards set forth in Point II, B (b), *infra*, pp. 40-48) and to be protected against an allowance inadequate and unrelated to real value, which would amount to a deprivation of property without due process of law.

In *U. S.* v. *New River Collieries*, 262 U. S. 341 (1923), the Court said at pages 343-344:

> "The ascertainment of compensation is a judicial function, and no power exists in any other department of the Government to declare what the compensation shall be or to prescribe any binding rule in that regard."

See also *Chicago, Milwaukee & St. Paul Railway Company* v. *Minnesota*, 134 U. S. 418 (1890), at pages 457, 458.

Furthermore, it is well settled that a statute under which an administrative body acts must always provide for a right of judicial review to determine whether the decision of the administrative body was contrary to law or to the evidence or without evidence to support it.

See:

Denver Union Stock Yard Co. v. *United States*, 57 Fed. (2d) 735 (D.C.D. Colo., 1932);

Tagg Bros. v. *United States*, 280 U. S. 420 (1930), at page 444.

B

Subsection (c)(12) of Section 77, if held to be applicable to the services and expenses of the Indenture Trustee, would be unconstitutional on the separate and additional ground that it would impair its property rights in violation of the Fifth Amendment of the Constitution of the United States.

(a) Congress has no power under its bankruptcy powers to impair vested property rights.

As shown under Point I (pp. 7-25, *supra*), under both the Indenture and the common law, the Indenture Trustee has a contract right to reasonable compensation and expenses and has a prior lien or charge therefor upon the mortgaged property. It is our contention that the Indenture Trustee has the right to have the amount, validity and priority of that contract right and lien determined exclusively by the Bankruptcy Court and charged by it against the mortgaged property, including the cash amounting to $475,127.71 now deposited under the Indenture, and that if Congress has attempted to substitute therefor the right to have the Commission determine the maximum amount of that right and lien under Section 77(c)(12), that statute, if applied to the Indenture Trustee, is an unconstitutional impairment of its vested property rights in violation of the Fifth Amendment to the Constitution. The District Court properly ordered the compensation and expenses of the Indenture Trustee to be paid from such deposited cash.

It is well settled that the bankruptcy power of Congress is subject to the Fifth Amendment and that, accordingly, Congress does not have the power to impair vested rights or liens by bankruptcy legislation.

See:

Louisville Bank v. *Radford*, 295 U. S. 555 (1935), at pages 589, 594, 601-602;

Continental Bank v. *Rock Island Ry.*, 294 U. S. 648 (1935), at pages 676-677, 681.

In *Security-First National Bank* v. *Rindge Land & Navigation Co.*, 85 Fed. (2d) 557 (C.C.A. 9, 1936), the Court said at page 561:

> "The right to retain a lien until the debt secured thereby is paid is a substantive property right which may not be taken from the creditor consistently with the Fifth and Fourteenth Amendments to the Constitution. *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, 594."

See to the same effect:

In re American Motor Products Corporation, 98 Fed. (2d) 774 (C.C.A. 2, 1938), at page 775;

In re Utilities Power & Light Corporation, 91 Fed. (2d) 598 (C.C.A. 7, 1937), at pages 600-601; cert. denied 302 U. S. 742;

Guaranty Trust Co. v. *Henwood*, 86 Fed. (2d) 347 (C.C.A. 8, 1936), at page 352; cert. denied 300 U. S. 661.

Nor does Congress have any power to impair vested property rights under its power to regulate interstate commerce since the latter power, like the bankruptcy power, is subject to the Fifth Amendment. See *Monongahela Navigation Co.* v. *United States*, 148 U. S. 312 (1893), at page 336, and other cases cited in footnote to page 589 of *Louisville Bank* v. *Radford*, 295 U. S. 555.

(1935), *supra*, at pages 589-590. Thus the invocation of the commerce power by the attorney for the Trustees of the New Haven Railroad (pp. 4-5 of his *Amicus Curiae* brief herein), requires no reply.

Petitioner fails to distinguish between the impairment of obligation of contract and the impairment of a vested property right. See *Louisville Bank* v. *Radford*, *supra*, at pages 589-590, where that distinction is made clear. We are not invoking the prohibition against impairment of obligation of contract, which we realize is not applicable to action by Congress. The cases of *Kuehner* v. *Irving Trust Co.* and *Philadelphia B. & W. R. Co.* v. *Schubert*, cited by Petitioner at page 28 of its Brief, are concerned solely with that matter and do not involve a lien or other property right and thus have no application to the case at bar. What we do contend is that Subsection (c)(12), if held to subject the Indenture Trustee's claim and lien to the jurisdiction of the Commission, would be an impairment of its vested property rights in violation of the Fifth Amendment of the Constitution.

(b) Section 77(c)(12), if applicable to the Indenture Trustee, would not be a mere suspension of or change in its remedy, but would be an impairment of its substantive property rights.

The District Court in the New Haven decision said (see pp. 63 and 66 of Appendix B of Petitioner's Brief):

> "The petitioners' liens are not impaired. Like the liens of all the mortgagees and pledgees in these proceedings, the remedy only is suspended. If these proceedings shall be dismissed, the lien forthwith becomes enforceable with all its pristine vigor. Such

a suspension of the remedy is not inconsistent with the Constitution."

. . . . . .

"Nor can the bankruptcy court in these proceedings enforce the petitioners' liens. For the liens are suspended during these proceedings: they may be enforced only if these proceedings are dismissed."

We submit that those conclusions are erroneous because an actual and serious impairment of substantive property right, and not a mere suspension of remedy, is involved.

This is shown by a comparison between the remedy of an "allowance to be paid out of the debtor's estate" provided for in Section 77(c)(12) under which the Commission would have sole power to fix the maximum limit of the Indenture Trustee's contract claim and lien and which would be subject to the other conditions and restrictions of that statute, set forth at pages 43-45 hereinafter, and the contractual right to reasonable compensation and expenses secured by a lien, the amount of which is to be adjudicated by the Bankruptcy Court. The difference between the two is so fundamental as substantially to lessen the value of that lien and to impair the Indenture Trustee's substantive property rights to a lien thereunder.

Under the provisions of the Indenture and under the common law:

(1) The Indenture Trustee has a contract right to reasonable compensation and expenses (including counsel's compensation and expenses), for all services rendered by it in the execution of the trust, secured by a lien or

charge upon the mortgaged property. This has been fully sustained by the District Court in the New Haven decision. (See pp. 59-61 of Appendix B of Petitioner's Brief.)

(2) It is entitled under the laws in force at the time the Indenture contract was entered into by the Indenture Trustee in 1903 and which became a part of the obligation, to have the amount and extent of that claim and lien adjudicated by a court, which will feel bound to exercise its independent judgment in measuring the value of the services of the Indenture Trustee and of its attorneys by standards which have long been properly employed by the courts in fixing compensation. Those standards include the difficulty and intricacy of the matters presented, the amount involved, the results attained, the time spent and the experience and qualifications of the persons properly performing such services (*In re Osofsky*, 50 Fed. (2d) 925 (D.C.S.D. New York, 1931), at p. 927).

(3) It is entitled to compensation and expenses for all services performed by it in the execution of the trusts created by the Indenture, irrespective of whether they were directly and materially beneficial to the estate as a whole and contributed directly and materially to the accomplishment of the reorganization. As stated by the Circuit Court of Appeals in its opinion in the case at bar (Rec. p. 106), the fact that the services of the Indenture Trustee on behalf of the trust estate were also beneficial to the reorganization proceedings should add to its right to compensation, rather than detract therefrom (*supra*, p. 6).

(4) It is entitled to a right of review by a court which has power to raise, as well as lower, the maximum limits fixed by the Commission.

Compared with the foregoing right to compensation and expenses to which the Indenture Trustee is entitled under its Indenture contract and lien, as well as under the common law, the right under Section 77(c)(12) (if applicable, which we deny) is not an effective equivalent, but an illusory substitute amounting to a deprivation of property.

Thus, under that statute:

(1) The Indenture Trustee is deprived of its absolute contract right to compensation, secured by a prior lien, for services in the execution of the trusts, and is given merely permission to ask the Commission for a discretionary allowance.

(2) It is deprived of its right to have the Court exercise its independent judgment in passing upon the amount of its claim according to definite standards and precedents which have been evolved and applied by the courts in fixing fair compensation for the last 150 years. Instead, it is subjected to the jurisdiction of the Commission to fix any maximum limits it pleases in its uncontrolled discretion and based upon standards not relevant in determining the lien claim of the Indenture Trustee, such as the exigencies of the plan of reorganization, the need of the Debtor for adequate cash working capital and the total of the allowances applied for.

(3) Its allowance is limited by the extent to which its services have directly and materially benefited the estate

as a whole or the plan of reorganization (as distinguished from those services which have benefited only its bondholders), since those are the standards which the Commission applies in fixing maxima under Subsection (c) (12).* It is deprived of its right to receive reasonable compensation for its services in the execution of the trusts created by the Indenture that did not directly and materially benefit the estate as a whole or aid in the consummation of the reorganization**, having been rendered

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* In the Supplemental Report of Division 4 of the Commission on the petitions for rehearing on compensation in the Missouri Pacific Railroad Company Reorganization, 247 I.C.C. 273 (June 30, 1941), the Commission said at page 278:

> "The doctrine has been clearly established that the debtor's estate should be charged with only such services as are found to have benefited it. *In re Chicago, Milwaukee, St. Paul & Pacific Railroad Company, Debtor*, United States Circuit Court of Appeals, Seventh Circuit, May 20, 1941. * * * We find that much of the time devoted by this petitioner in the performance of its services did not benefit the general estate of the debtor."

See to the same effect: *Savannah & Atlanta R. Co. Reorganization*, 228 I.C.C. 543 (1938), at page 558, and *Erie Railroad Company Reorganization Supplemental Report of Division 4, November 15, 1940*, at page 4.

** Thus, it has been established that services performed for the benefit of a particular party or group and which did not benefit the Debtor's estate as a whole are not compensable under Section 77(c)(12). See *New York, New Haven and Hartford Railroad Company Reorganization*, 247 I.C.C. 677 (August 27, 1941) at page 764, in which the Commission denied an allowance under Section 77(c)(12) to a holder of debentures of a subsidiary of the Debtor for counsel fees, saying:

> "All of the activities of the petitioner in these proceedings, in our opinion, were primarily in their own interest and behalf. We find that neither the estate of the principal debtor nor that of the Old Colony was benefited by them. Accordingly, we are unable to fix maximum limits of allowances therefor in these proceedings."

and incurred exclusively for, and resulting in the benefit and protection of a particular group—the holders of the Bonds secured by the Indenture.

(4) It is not entitled to any right of review by a court which has the power to raise, as well as lower, the maximum limits fixed by the Commission, to which it is constitutionally entitled.

In view of the foregoing it is difficult to find any basis whatsoever for the conclusion of the District Court in the New Haven decision (see p. 62 of Appendix B of Petitioner's Brief) that the same standard of liquidation prevails under Section 77(c)(12) as under the Indenture contract.

We submit that the Commission, by its own admission, has made it abundantly clear that the two standards of liquidation are not the same. Thus in the compensation report of Division 4 of the Commission in the New York, New Haven and Hartford Railroad Company Reorganization, 247 I.C.C. 677 (August 27, 1941), it was stated at page 696:

> "Finally, from all of the foregoing, we believe it is clear that we are not fixing the maximum limits of allowances for services and expenses of mortgage trustees on the basis of the indenture contracts."

Certainly the use of the word "reasonable" in both the statute and the Indenture does not make the two standards of liquidation the same, when, as shown herein, the standards employed by the Court and those employed by the Commission, in determining reasonableness are so fundamentally different. No more persuasive proof of that difference and that the Indenture Trustee would suffer a serious injury to its property rights under the

standards applied by the Commission, can be found than by a comparison between the amounts of compensation granted by the District Court and of the maxima of allowances set by the Commission in this very case. Thus, while the District Court granted compensation (which it necessarily must have regarded as reasonable) in the sums of $10,000 to the Indenture Trustee, $10,000 to White & Case, and $6,000 to Bryan, Williams, Cave & McPheeters, the maximum allowances fixed by the Commission for those services were $2,500, $3,500 and $2,000, respectively, aggregating less than one-third of the total compensation granted by the Court. The Circuit Court of Appeals recognized that this large discrepancy between the amount of compensation granted by the Court and the amount of allowances granted by the Commission, was due to a difference between the standards of compensation applied by the Commission and those applied by the Court. Thus it stated in its opinion (Rec. p. 107):

> "* * * But the Commission was measuring the reasonable value of appellee's services in the reorganization proceedings to the estate of the debtor. Appellee is not asking for compensation for that service. On the other hand it asks reasonable compensation for the value of its services to the trust estate. We find nothing in the record which would justify us in overruling the decision of the bankruptcy court upon the necessity or propriety of the services rendered by the appellee to the trust estate nor upon the value of the services rendered."

Surely these results all show conclusively that something much more fundamental than the method and forum for determining compensation is altered if Section 77(c)-(12) is substituted for the rights of the Indenture Trustee under its contract and lien.

In this connection also we call the Court's attention to the fact that the statistics set forth at page 12 of the Petition for Writs of Certiorari in this case show that the standards of compensation employed by the Commission seem to be particularly prejudicial to indenture trustees. The maxima allowed to them in nine reorganization proceedings set forth at page 27 of that Petition have aggregated only 37.4 per cent of their claims, as compared with aggregate allowances of 47.9 per cent of the amounts claimed by all parties (excluding compensation and expenses of debtor's trustees, and expenses of reorganization managers). Furthermore, this discrepancy would be considerably greater if indenture trustees had been excluded in computing the above figure of 47.9 per cent. It is our belief that this substantially lower rate of compensation awarded to indenture trustees is undoubtedly due to the failure of the Commission to grant adequate compensation to them for their services which benefited the trust estate and the bondholders, but which were not beneficial to the debtor's estate as a whole or the reorganization. This belief is substantiated by the statement of Petitioner in its brief (p. 34) that the Commission is in a position to apply a uniform standard in fixing maximum allowances. That standard is, as has been shown at pages 43-44, *supra*, benefit to the debtor's estate as a whole and to the plan of reorganization. No clearer proof of injury to the property rights of indenture trustees could be found than the uniform application of that standard in determining the value of their services to the trust estate and to their bondholders.

If Petitioner's contention that the Commission is peculiarly qualified to pass on the maximum allowances (pp. 33-34 of its Brief) is intended to refer to indenture trustees and their attorneys, we strongly disagree with it.

Except in unusual circumstances, by far the larger part of an indenture trustee's services are performed entirely before the Court, which alone has first-hand knowledge of their extent and value, and only a relatively small proportion is performed before the Commission. For example, see the opinion of the District Court of Connecticut in *In re New York, New Haven and Hartford Railroad Company, Debtor*, 46 Fed. Supp. 214 (U.S.D.C. Conn., June 3, 1942), at pages 228 to 236.

It is clear from all of the foregoing that the substitution of Section 77(c)(12) for the rights of the Indenture Trustee under its Indenture contract and under the common law is not a mere change in the mode of procedure of liquidating its compensation, but is a serious injury to its substantive property rights in that the substitute remedy under that statute is not substantial and efficient within the requirement of *Crane* v. *Hahlo* at page 147 and *Hardware Dealers' Mutual Fire Insurance Co.* v. *Glidden* at page 159, Petitioner's Brief, pp. 34-35. That injury is not changed one iota by the District Court's reminder in the New Haven decision that "*if*" the reorganization proceedings are dismissed, the Indenture Trustee's lien becomes enforceable.

C

Subsection (c)(12) of Section 77, if held to be applicable to the services and expenses of the Indenture Trustee, would also be a violation of Section I of Article III of the Constitution of the United States.

In the event that Subsection (c)(12) is held to apply to compensation and expense of an indenture trustee with a contract claim and lien therefor against the mortgaged property, it is a violation of Section I of Article III of the United States Constitution.

Under Section I of Article III of the Constitution, the judicial power of the United States is vested exclusively in the Courts. Thus in matters involving private right the judicial power may not be delegated to bodies other than constitutional courts.

The adjudication of the amount of the contract claim and lien of an indenture trustee for its compensation and expenses is clearly a matter of private right and a judicial function which can be perforined only by the courts. Functions traditionally performed only by courts are deemed within the judicial power of the United States. *Crowell* v. *Benson*, 285 U. S. 22 (1932), at page 51; *Murray* v. *Hoboken Land and Improvement Company*, 18 How. 272 (1855).

Furthermore, no standards whatsoever are set up in Section 77(c)(12) or Section 77(e)(2) for the determination of maxima by the Commission or for fixing reasonable value.

There is a clear distinction between indenture trustees and volunteers in Section 77 proceedings. Unlike the former, the latter are not under any preexisting duties and responsibilities and may limit the extent and nature of their services or may be willing to take their chances on Court allowances within a maximum to be fixed by the Commission. They have no contract claim and lien for compensation for their services. The amounts of their allowances and the method of determining the same can, of course, be fixed by Congress in the statute which creates their right thereto. Section 48 of the Bankruptcy Act and the cases of *Callaghan* v. *Reconstruction Finance Corporation*, 297 U. S. 464 (which did not involve any determination by an administrative body), *Calhoun* v. *Massie*, 253 U. S. 170, and *Margolin* v. *U. S.*, 269 U. S. 93 (Petitioner's Brief, p. 34), all fall within the latter category and are not relevant here.

Since Section 77(c)(12), if applicable, gives a body other than a constitutional court power to make a final decision as to maximum allowances for services and expenses covered by a pre-existing contract claim, secured by a lien, as to which there is no right of court review and no prescribed standards, it is contrary to Section I of Article III of the Constitution.

The constitutionality of the statute should be upheld by holding that Section 77(c)(12) is not and was not intended to be applicable to an indenture trustee having a contract right and lien for compensation for its services and expenses in the execution of the trusts.

CONCLUSION

The judgment of the Circuit Court of Appeals should be affirmed.

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Respectfully submitted,

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